

(Without Reference to File)

SENATE THIRD READING

SB 125 (Committee on Budget and Fiscal Review)

As Amended June 12, 2026

2/3 vote. Budget Bill Appropriation Take Effect Immediately

SUMMARY

This budget trailer bill implements the Managed Care Organization tax as component of the Budget Act of 2026.

Major Provisions

This budget trailer bill implements the Managed Care Organization tax as a component of the Budget Act of 2026.

Specifically, this bill:

- 1) States legislative intent to implement a Managed Care Organization (MCO) provider tax that is not subject to the Protect Access to Health Care Act of 2024 and that meets certain goals, including compliance with federal requirements and funding for the Medi-Cal program.
- 2) Imposes an MCO provider tax on a health plan, as defined, for the 2027, 2028, and 2029 calendar years.
- 3) Prohibits the department from collecting the tax until the Director of Health Care Services certifies that the tax is a federally permissible health care-related tax meeting specified federal requirements, or until the department receives federal approval that the tax is a permissible health-care related tax, as specified.
- 4) Sets the tax amount at \$8.85 per countable enrollee per month, unless that amount is modified by the department under certain conditions.
- 5) Establishes the Medi-Cal Stability Fund, and deposits the tax revenues, less refunds, in that fund.
- 6) Clarifies that deposited funds would be continuously appropriated to the department for the purpose of funding the department's administrative costs, the nonfederal share of increased capitation payments to Medi-Cal managed care plans, the nonfederal share of certain Medi-Cal payments, and the nonfederal share of Medi-Cal managed care rates for certain health care services, as specified.
- 7) Requires the Department of Health Care Services to request federal approval as is necessary to implement these MCO provider tax provisions.
- 8) Sets forth various procedures regarding the inoperative status of these provisions if the tax was determined to be noncompliant or was rejected, as specified.

- 9) Makes the MCO provider tax provisions inoperative on January 1, 2031, and would repeal them on January 1, 2032, with an exception for certain provisions relating to the Medi-Cal Stability Fund.

COMMENTS

- 1) AB 119 (Budget Committee) of 2023, as amended by SB 136 (Budget and Fiscal Review) Chapter 6, Statutes of 2024 and AB 160 (Budget Committee) Chapter 39, Statutes of 2024, authorized an enrollment-based MCO tax from April 1, 2023 through December 31, 2026. Under the current MCO tax structure, Medi-Cal enrollment is taxed at a significantly higher rate than commercial enrollment, requiring the state to obtain a federal waiver from federal proportionality rules. That waiver, and the current tax structure, are approved through the end of December 2026.
- 2) California's current MCO tax generates between \$7 billion and \$8 billion in net revenue annually, with most of the funding to date offsetting General Fund spending in Medi Cal. The smaller remaining share of funding supports certain programmatic augmentations, primarily Medi-Cal provider rate increases.
- 3) Proposition 35 (November 2024) governs how MCO tax revenue is spent beginning in 2025 and requires the state to continue a substantially similar tax on and after January 1, 2027.
- 4) H.R. 1 (Public Law No. 119-21, 139 Stat. 72) significantly constrains state options to impose health care-related taxes and prohibits taxes that assess higher tax rates on Medi-Cal plans than commercial plans or otherwise place a disproportionately high tax burden on Medi-Cal plans, making California's current MCO tax structure federally impermissible after December 31, 2026. A CMS final rule published February 2, 2026 codified these requirements and confirmed the December 31, 2026 transition deadline.
- 5) A key change from H.R. 1's new rules is that any renewed MCO tax must apply a uniform rate across Medi-Cal and commercial enrollment. Because commercial plans currently pay significantly less under the existing structure, a uniform rate means commercial plans will face a much higher per-enrollee tax than they pay today.
- 6) According to the Administration, the Department of Health Care Services (DHCS) will seek federal approval of a substantially similar MCO tax as required by Proposition 35 by no later than December 31, 2026. The federal government is expected to decline to approve this tax upon determining that it does not conform with H.R. 1 requirements. DHCS proposes to establish and concurrently seek federal approval to continue an alternative, federally compliant MCO tax effective January 1, 2027, in order to maintain ongoing support for the Medi-Cal program.

According to the Author

Arguments in Support

None on file.

Arguments in Opposition

None on file.

FISCAL COMMENTS

DHCS proposes to establish and concurrently seek federal approval to continue an alternative, federally compliant MCO tax effective January 1, 2027, in order to maintain ongoing support for the Medi-Cal program, as outlined below:

- 1) DHCS's costs of administering the MCO tax and associated expenditures not to exceed \$4 million annually;
- 2) The nonfederal share of increased capitation payments to Medi-Cal managed care plans (MCPs) accounting for their projected tax obligation;
- 3) The nonfederal share of sustaining 2024 targeted rate increases for primary, maternal, and behavioral health services at 87.5 percent of applicable Medicare rates, currently estimated at about \$300 million annually; and
- 4) The nonfederal share of Medi-Cal managed care rates for health care services furnished to children, adults, seniors and persons with disabilities, and persons dually eligible for the Medi-Cal program and the Medicare Program, in the amount of at least \$2 billion annually.

This bill would include a change in state statute that would result in a taxpayer paying a higher tax within the meaning of Section 3 of Article XIII A of the California Constitution, and thus would require for passage the approval of 2/3 of the membership of each house of the Legislature.

This bill would declare that it is to take effect immediately as a bill providing for appropriations related to the Budget Bill.

VOTES

SENATE FLOOR: 28-10-2

YES: Allen, Archuleta, Arreguín, Ashby, Becker, Blakespear, Cabaldon, Caballero, Cervantes, Cortese, Durazo, Gonzalez, Grayson, Hurtado, Laird, Limón, McGuire, McNERNEY, Menjivar, Padilla, Pérez, Richardson, Rubio, Smallwood-Cuevas, Umberg, Wahab, Weber Pierson, Wiener
NO: Alvarado-Gil, Choi, Dahle, Grove, Jones, Niello, Ochoa Bogh, Seyarto, Strickland, Valladares

ABS, ABST OR NV: Reyes, Stern

UPDATED

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